

VZCZCXRO6454
RR RUEHCHI RUEHDT RUEHHM RUEHNH
DE RUEHGP #1942/01 2960147
ZNR UUUUU ZZH
R 230147Z OCT 07
FM AMEMBASSY SINGAPORE
TO RUEHC/SECSTATE WASHDC 4273
INFO RUCPDOG/USDOC WASHDC
RUCNASE/ASEAN MEMBER COLLECTIVE

UNCLAS SECTION 01 OF 02 SINGAPORE 001942

SIPDIS

DEPT OF TREASURY WASHDC
STATE PASS TREASURY SSEARLS

SIPDIS

E.O. 12958: N/A

TAGS: [EFIN](#) [ECON](#) [ETRD](#) [EFIN](#) [EINV](#) [SN](#)

SUBJECT: Singapore Moves to Fight Inflation

1. (U) Summary. After a summer surge in prices, the Monetary Authority of Singapore (MAS) finally moved to combat the island's inflationary spike. MAS hopes that by accelerating the appreciation of the currency, it will be able to bring inflation back within its long term target range of below 2 percent. Analysts were surprised at the change in currency policy, but remain somewhat concerned that the measure may not go far enough to slow price increases in non-tradable goods and services such as property. End summary.

Inflation at 13-year High

2. (U) MAS acknowledged the increased upward pressures on inflation in its twice annual statement on October 10. Inflation has accelerated from 0.8 percent on a year-on-year basis in the first half of 2007 to 2.8 percent year-on-year in the July-August period -- its highest level in more than 13 years (see Table 1). Half of this acceleration could be attributed to July's one-off hike in the goods and services tax (i.e. value added tax), according to MAS. The rest came from robust economic growth, low unemployment, severe shortages in commercial, office and residential space, and large jumps in asset prices. MAS expects inflation to come in at 1.5-2.0 percent in 2007 and 2.0-3.0 percent in 2008. Based on the hawkish tone of the monetary policy statement, concerns about inflation appear now to be MAS's focus rather than economic growth.

Table 1. Singapore's Inflation

	Consumer Price Index	Percentage Change Year-on-year
1997	96.2	2.0
1998	95.9	-0.3
1999	96.0	0.0
2000	97.2	1.3
2001	98.2	1.0
2002	97.8	-0.4
2003	98.3	0.5
2004	100.0	1.7
2005	100.4	0.5
2006	101.4	0.5
January 07	101.3	0.2
February 07	101.9	0.6
March 07	101.7	0.7
April 07	102.1	0.6
May 07	102.4	1.0
June 07	102.0	1.3
July 07	104.1	2.6
August 07	104.5	2.9

Unique Monetary Policy Instruments

13. (U) As a small, open economy, Singapore operates on the premise that most inflation will be imported from overseas. As such, MAS uses the exchange rate as its primary tool to fight inflation, rather than the interest rate as in most countries. Technically, MAS does this by intervening in the foreign exchange market to keep the exchange rate within an undisclosed band versus a trade-weighted average nominal exchange rate, known as the Singapore dollar nominal effective exchange rate (S\$NEER). MAS does not disclose either the exact weights of the currencies used in the S\$NEER or the width or slope of the band of allowable changes for the Singapore dollar versus the S\$NEER. MAS uses its twice annual policy statements to describe the general trend of its currency policy and any changes it intends to make to the intervention band.

New Policy Tightens Monetary Policy

14. (U) MAS's October 10 policy statement did not change its general characterization of its currency policy: it maintained "the gradual and modest appreciation of the Singapore dollar nominal effective exchange rate (S\$NEER)." However, MAS surprised the market by announcing it would increase "slightly the slope of the S\$NEER policy band." The change in the slope of the intervention band suggests greater scope for the Singapore dollar to rise in the future. Singapore, therefore, is tightening its monetary policy to combat inflation.

12. (U) Market analysts expect this change to translate into 2 to 3 percent annual appreciation of the S\$NEER compared to

SINGAPORE 00001942 002 OF 002

previous estimate of 1.5 to 2.5 percent. This should bring the exchange rate to S\$1.46-1.47 per U.S. dollar in 2007, and to S\$1.39-1.44 per U.S. dollar in 2008. Nevertheless, some market analysts expect the effect of this tighter monetary policy bias to be limited in the near term. In addition to further fine tuning of its monetary policy, MAS may also require non-monetary policy measures in 2008 to contain inflationary pressures.

Comment: Will It Be Enough?

13. (U) While MAS surprised the market by changing its currency policy, it remains to be seen if this minor adjustment will be enough to rein in inflation. The high rate of inflation in non-tradable goods (such as rents and services) raises the possibility that the exchange rate will be less effective than in the past at slowing Singapore's overall inflation. End
Comment.

HERBOLD